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# **The Impact of the Political Cycle on House Prices: The Australian Experience**

## **Abstract**

In several countries, high house prices have emerged as a significant social and economic issue. This exploratory study examines if house prices can be linked to the political cycle, specifically at election time, as governments realise homeowners represent a large voter base and house price movements will influence their voting intentions. To examine this relationship, the research utilizes 40 years of quarterly Melbourne house price data to examine the relationship between the movement in real house prices one year before and after local (State government) and national (Federal government) elections.

Over the last four decades, Melbourne quarterly real house prices increased by 1.24% (annualised 5.05%). One year before an election, on average, the quarterly real house price increased by 1.21% Federal and 2.33% State. This compared to one year post election of 0.84% Federal and 0.60% State. At State government election time, depending on the political parties, there is a divergence on house price movement. As this research clearly identifies major variations in house price performance around election time, residential property decisions should make reference to the political cycle.

Key words: residential house prices, political studies, property cycles

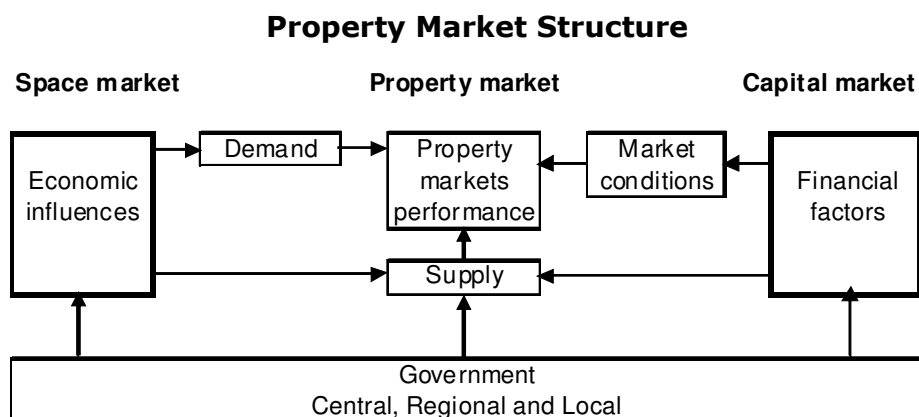
# The Impact of the Political Cycle on House Prices: The Australian Experience

## 1. Introduction

Clearly housing is more than a unique and valuable investment asset class. It is a key component of society wellbeing, in providing shelter and as a source of economic activity. As housing is an important component of a country's prosperity, controlling the various aspects of housing is clearly a core long-term government mandate.

In acknowledging government's responsibilities for housing, the type and timing of policies across various levels of government can have far reaching effects on house prices. The extent of the government policies can be illustrated by examining the structure of the property market, with reference to the Figure 1 established three-market model which shows the relationship of the property, space and capital markets.

*Figure 1*



Adapted: Archer and Ling 2007

Figure 1 illustrates governments' influences across the property, space and capital markets. Government policy examples which can impact on house prices are as follows:

- i. Space market (Demand)
  - Population policies (quotas on overseas migration)
  - First time home buyers, incentives
  - Opportunities for overseas owners to purchase residential properties
- ii. Capital market (Finance)
  - Monetary policies (money supply, government bonds)
  - Changes in property taxes (negative gearing, transaction tax - stamp duty)
  - Regulations that impact on alternative asset classes
  - Changes in superannuation policies (in an indirect way)
- iii. Property market (Property market conditions and supply)
  - Release/rezoning of new residential land
  - Changes in planning policies (housing density)
  - Building regulations (sustainability agenda)

In detailing government housing policies, policy timing and implementation can be used to manage and stimulate the housing market. The impact of these policies on house prices could be gradual or immediate. As home owners represent a large percentage of the voter base those policies implemented close to an election may influence their voting intention. If a link can be established, future research on house price movement may relate less to traditional property cycle features and more to the political cycle.

The purpose of this research is to study the behaviour of house prices under various national and local political environments. This can be achieved by examining real house price performance over time for a specific residential property market. For this research Melbourne house prices was used as a representative case study. In grouping house price movement before and after elections, the impact of the political cycle can be compared to long term real residential property returns.

It should be noted that this research is not intended to endorse particular political parties, but rather to illustrate an approach for evaluating the impact of the political cycle on house prices. Similarly, it is outside the scope of this research to examine specific political factors which have impacted house prices.

Following this introduction, Section two provides a literature review on housing and political cycles. Section three details the selected residential property market data with national (Federal) and local (State) political elections and the research methodology. Section four provides the empirical findings and the implications. The last section provides the concluding comments.

## **2. Literature Review**

Economic theory has evolved, with major milestones providing new ways of thinking about the nature and theory of managing economic markets. Work by Marx (1867), Keynes (1936) and Friedman (1962) have introduced new concepts that have shaped economic strategies.

Importantly, Keynes (1936) acknowledged the role of government to use all powers at their disposal to influence aggregated demand. Governments have available fiscal measures including changes in tax rate and spending alongside monetary measures associated with the management and supply of money.

In providing the tools to manage the economy, government actions may be politically motivated to assist in the election of governments. Nordhuas (1975) presented the “*Political Business Cycle*” whereby suggesting government policies can manipulate the economy for electoral gain. These have been identified in three key areas:

- i. Macroeconomic outcomes: economic growth, lower inflation and lower unemployment etc
- ii. Beneficial rewards: voter tax breaks etc
- iii. Monetary policy: money supply and interest rates (in some countries interest rates are set independently by an appointed organisations, for example: Bank of England, Reserve Bank of Australia).

Source: Ladewig (2008)

In detailing government strategies that can affect the political business cycle, there is criticism that the literature is often theoretically and empirically weak surrounding these key areas (Drazen 2000, Keech 1995 and Suzuki 1991).

Contrary to the debatable links to the economy, research, particularly in the US, has coupled the political business cycle to investment asset classes. The relationship to equity and bond markets is centred on the performance of the asset classes, with reference to the political parties that were in power. The research provides conflicting evidence as to which political party provided overall better returns (Powell *et al* 2007, Ramchander *et al* 2009, Santa Clara and Valkanov 2003).

For Australia and New Zealand, Anderson *et al* (2008), extended the political cycle literature by considering the links between governments and the equities, bonds, and property markets. The findings suggest that all asset markets are affected by the inflationary effects of government policies. These differential inflationary patterns have consequences for investment markets, with property offering a natural hedge to inflation. The study did note that the differences in nominal returns, real returns and market risk premiums for the property market were insignificant across the Australian Federal government parties.

Alternatively, Abelson *et al* (2004), looked to explain real house prices movement over the long term (1970-2003). Significantly, the research discovered a broad range of real house prices determinants (inflation, unemployment, mortgage rates and the supply of housing) all which are affected to a greater or lesser degree by government policies.

Berry and Dalton (2004) likewise commented on the security of a “*bricks-and-mortar*” investment being supported in the past and continued to be influenced by government housing and social policies. The persistence of government policy interventions can change housing market outcomes with a range of effects, some being unintended and some contradictory.

In summary, many house price drivers are linked to government macroeconomic policies, which are made within a political framework. Consequently, in this environment, housing outcomes, although difficult to validate, can be an important election vote winner as home owners represent a large voter base.

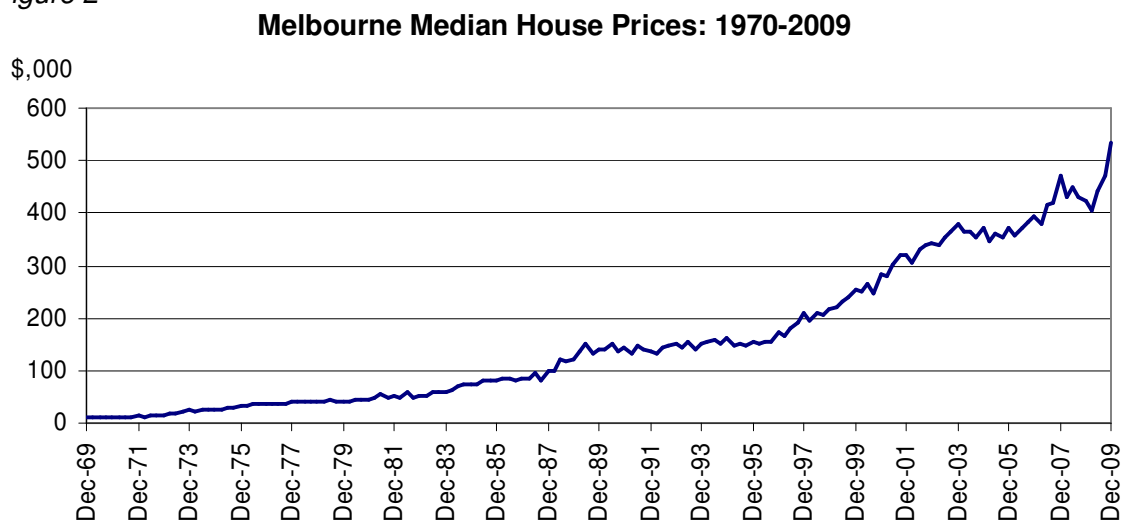
### 3. Data and Methodology

#### 3.1 Data

Across Australia, determinants of the residential property markets can vary with local influences. For example in spring 2009, both the Perth and Brisbane residential property markets were performing above other State capitals, as these cities are associated with the booming resource sector (ANZ 2009).

In looking at a specific housing market, State and Federal political cycles can be compared to residential property market movement. In Melbourne, the *Real Estate Institute of Victoria* collects and publishes established median house prices. Combined with an extended database from *BIS Shrapnel* a quarterly 1970 to 2009 Melbourne median house data series was created. Figure 2 details the Melbourne median house price over the last 40 years.

Figure 2



Source: REIV 2010, BIS Shrapnel 2009

Figure 2 illustrates the movement in Melbourne median house prices. The quarterly house price movement represents 2.65% (annualised 11.05%). The level of movement varies over time with substantial growth occurring during the last decade, particularly over the last 12 months.

In detailing Melbourne median house price movement, annualised Melbourne inflation ranged -0.4% to 17.7% over this time period. The changes in inflation would impact on

comparing different time periods. Therefore the research examined real house price movement with inflation removed.

The democratic political system in Australia comprises three tiers of government. Key political decisions are at Federal and State levels, with Local government generally being responsible for community services. The elections for Federal and most State governments are held on a three yearly basis with compulsory voting for those over 18 years of age.

A break down of the Australian political system and the government responsibilities is shown in Table1.

*Table 1*

**Australian Government Responsibilities for the Economy**

<b>Level of government</b>	<b>Economic Infrastructure</b>	<b>Social Welfare</b>
<b>Commonwealth Government</b>	<ul style="list-style-type: none"> <li>- Aviation</li> <li>- Telecommunication and post</li> <li>- National highways</li> </ul>	<ul style="list-style-type: none"> <li>- Tertiary education</li> <li>- Public housing (shared)</li> <li>- Health facilities (shared)</li> </ul>
<b>State Government</b>	<ul style="list-style-type: none"> <li>- Roads (rural, urban, local)</li> <li>- Railways</li> <li>- Ports</li> <li>- Electricity supply</li> <li>- Dams, water, sewerage</li> <li>- Public transport (train, bus)</li> </ul>	<ul style="list-style-type: none"> <li>- Education institutions</li> <li>- Childcare facilities</li> <li>- Community health facilities</li> <li>- Public housing (shared)</li> <li>- Sport and recreational facilities</li> <li>- Cultural facilities</li> <li>- Libraries</li> <li>- Public order and safety</li> </ul>
<b>Local Government</b>	<ul style="list-style-type: none"> <li>- Roads (rural, urban, local)</li> <li>- Sewage treatment</li> <li>- Water supply and drainage</li> <li>- Electricity supply</li> </ul>	<ul style="list-style-type: none"> <li>- Childcare centres</li> <li>- Libraries</li> <li>- Community centres</li> <li>- Nursing homes</li> <li>- Recreational facilities</li> <li>- Open spaces</li> </ul>

Source: Higgins et al, 2007

The Australian political system is dominated by two parties, Liberal (Conservatives) and Labor (Democrats). Table 2 and Table 3 show the respective Federal and State Governments and the election dates. To coincide with the quarterly property data, the election dates are shown on a quarterly basis.



Table 2

## Federal Government and Election Details

Prime Minister	Party in government	Election Quarter	Assumed Office	Retired from Office	Period of service (Quarters)
<b>John Gorton</b>	<b>Liberal Party*</b>		<b>Dec-68</b>	<b>Mar-71</b>	<b>13</b>
		Dec-66 Sep-69	Sep-69	Mar-71	5
<b>William McMahon</b>	<b>Liberal Party*</b>		<b>Mar-71</b>	<b>Dec-72</b>	<b>7</b>
<b>Gough Whitlam</b>	<b>Labor Party</b>		<b>Dec-72</b>	<b>Dec-75</b>	<b>12</b>
		Dec-72 Jun-74	Dec-72 Jun-74	Jun-74 Dec-75	6 6
<b>Malcolm Fraser</b>	<b>Liberal Party*</b>		<b>Dec-75</b>	<b>Mar-83</b>	<b>29</b>
		Dec-75 Dec-77 Sep-80	Dec-75 Dec-77 Sep-80	Dec-77 Sep-80 Mar-83	8 11 10
<b>Bob Hawke</b>	<b>Labor Party</b>		<b>Mar-83</b>	<b>Dec-91</b>	<b>35</b>
		Mar-83 Dec-84 Jun-87 Mar-90	Mar-83 Dec-84 Jun-87 Mar-90	Dec-84 Jun-87 Mar-90 Dec-91	7 10 11 7
<b>Paul Keating</b>	<b>Labor Party</b>		<b>Dec-91</b>	<b>Mar-96</b>	<b>17</b>
		Mar-93	Dec-91 Mar-93	Mar-93 Mar-96	5 12
<b>John Howard</b>	<b>Liberal Party*</b>		<b>Mar-96</b>	<b>Dec-07</b>	<b>47</b>
		Mar-96 Sep-98 Dec-01 Sep-04	Mar-96 Sep-98 Dec-01 Sep-04	Sep-98 Dec-01 Sep-04 Dec-07	10 13 11 13
<b>Kevin Rudd</b>	<b>Labor Party</b>		<b>Dec-07</b>	<b>-</b>	<b>8</b>

\* Coalition government.

Table 2 details the elected Australian Prime Ministers for the past 40 years. The three yearly electoral cycle has produced 16 elections over the period leading to 7 changes of government. The shortest period of government was the William McMahon lead government (20 months), compared to John Howard lead government of over 10 years, having been re-elected three times.

The Victorian State Government and election dates are show in Table 3.

Table 3

## Victorian State Government and Election Details

Premier	Party in government	Election Quarter	Assumed Office	Retired from Office	Period of service (Quarters)
<b>Henry Bolte</b>	<b>Liberal Party*</b>		<b>Jun-55</b>	<b>Sep-72</b>	<b>69</b>
		Jun-55 Jun-58 Jun-61 Jun-64 Mar-67 Jun-70	Mar-67 Jun-70	Jun-70 Sep-72	13 12
<b>Rupert Hamer</b>	<b>Liberal Party</b>		<b>Sep-72</b>	<b>Jun-81</b>	<b>35</b>
		Jun-73 Jun-76 Jun-79	Sep-72 Jun-73 Jun-76 Jun-79	Jun-73 Jun-76 Jun-79 Jun-81	3 12 12 8
<b>Lindsay Thompson</b>	<b>Liberal Party</b>		<b>Jun-81</b>	<b>Mar-82</b>	<b>3</b>
<b>John Cain</b>	<b>Labor Party</b>		<b>Mar-82</b>	<b>Sep-90</b>	<b>32</b>
		Mar-82 Mar-85 Sep-88	Mar-82 Mar-85 Sep-88	Mar-85 Sep-88 Sep-90	12 12 8
<b>Joan Kirner</b>	<b>Labor Party</b>		<b>Sep-90</b>	<b>Sep-92</b>	<b>9</b>
<b>Jeff Kennett</b>	<b>Liberal Party*</b>		<b>Sep-92</b>	<b>Sep-99</b>	<b>28</b>
		Sep-92 Mar-96	Sep-92 Mar-96	Mar-96 Sep-99	14 14
<b>Steve Bracks</b>	<b>Labor Party</b>		<b>Sep-99</b>	<b>Jun-07</b>	<b>31</b>
		Sep-99 Dec-02 Dec-06	Sep-99 Dec-02 Dec-06	Dec-02 Dec-06 Jun-07	13 16 2
<b>John Brumby</b>	<b>Labor Party</b>		<b>Jun-07</b>	<b>-</b>	<b>10</b>

\* Coalition government.

Table 3 shows that for the last 40 years, there have been 16 Victorian State elections with 8 Premiers. The shortest period of government was the Lindsay Thompson lead government of 9 months, whilst Robert Hamer was in power for over 9 years and re-elected four times.

### 3.2 Methodology

To examine the relationship between the political cycle and house price movement, the data was initially examined using descriptive analysis over each decade of the past 40 years. In addition, the performance during each elected Federal and State political party was examined over the time period.

In analysing the performance of the political parties, the political cycle can be examined using the performance of Melbourne house prices one year before and one year post election. An important consideration while interpreting the results is that the data only accounts for governments that have served more than 18-month post election period.

In testing the robustness of the results, the analysis compared different performance periods over the dataset. Statistical significance tests provided inconclusive evidence that the means of the two groups were statistically different. It is possible that any house price movement and the political cycle relationship are simply due to co-movements with external factors, for example, global financial crisis and natural disasters.

#### 4. Results

The first step was to review the descriptive statistics for the Melbourne residential property market over 10-year intervals. This is shown in Table 4.

*Table 4*

**Melbourne Real House Prices Descriptive Statistics  
Quarterly Data: Jan 70 – Dec 09**

	1970's	1980's	1990's	2000's	Total
Mean	0.89%	1.54%	1.13%	1.28%	1.24%
Median	0.32%	1.41%	1.00%	1.63%	0.84%
Standard Deviation	6.41%	9.22%	5.91%	5.83%	6.91%
Kurtosis	- 0.03	0.41	- 0.87	- 0.31	0.57
Skewness	0.49	0.01	- 0.21	0.13	0.11
Range	26.20%	42.44%	21.40%	24.12%	42.44%
Minimum	-10.10%	-18.99%	-10.40%	-10.15%	-18.99%
Maximum	16.10%	23.45%	11.00%	13.98%	23.45%

Table 4 shows that over the last four decades, the average quarterly percentage change in Melbourne real house price ranged from 0.89% to 1.54%. The 1980's provided strong returns, being 30% above the long-term trend. House price movement over the last decade was very close to the long term average.

In each decade, low skewness and low kurtosis readings demonstrate a flat bell curve as illustrated by high standard deviation readings above 5%, with a wide data range of between -10% and 10%. This illustrates that movements in residential property market can be substantial and unrelated to movement in inflation.

The descriptive statistics for Melbourne house price performance under different Federal and State political parties is shown in Table 5.

*Table 5*

**Melbourne House Prices Descriptive Statistics  
Federal and State Political Parties  
Quarterly Data: Jan 70 - Dec 09**

	Federal Labor	Federal Liberal	State Labor	State Liberal	Overall
Mean	1.31%	1.18%	1.40%	1.07%	1.24%
Median	1.69%	0.69%	1.74%	0.52%	0.84%
Standard Deviation	7.51%	6.43%	7.32%	6.49%	6.91%
Kurtosis	0.58	0.48	0.87	0.07	0.57
Skewness	0.12	0.07	0.06	0.15	0.11
Range	42.44%	34.48%	42.44%	33.35%	42.44%
Minimum	-18.99%	-16.74%	-18.99%	-15.62%	-18.99%
Maximum	23.45%	17.74%	23.45%	17.74%	23.45%
Count	72	89	83	78	160

Table 5 details a relatively narrow quarterly house price range, 1.07% to 1.40%, for the Federal and State political parties. This represents a relative difference of  $\pm 16\%$  from the long term average of 1.24%. The difference in median values and to a lesser extent the standard deviation would suggest that Liberal Federal and State governments have consistently less volatile returns to that of Labor Federal and State governments. Although across the Federal and State political parties, similarities appear to be evident with low skewness and low kurtosis readings. This data tends to illustrate no significant variation / differences in the Melbourne house price performance either under the Labor Party or Liberal Party rule at both Federal and State government levels.

Table 6 compares the Melbourne house price performance during the first year of government by the Labor Party and the Liberal Party after each election at both Federal and Victoria State government level.

Table 6

**Federal and State Governments First Year Election Performance  
Melbourne House Prices: Quarterly Data**

<b>First Year</b>	Federal Labor	Federal Liberal	Federal Total	State Labor	State Liberal	State Total
Quarters	24	32	56	24	24	48
Mean	0.77%	0.89%	0.84%	1.25%	-0.04%	0.60%
Std. Dev	9.27%	6.01%	7.50%	7.56%	6.14%	6.85%

Table 6 illustrates nominal differences in Melbourne house price performance during the first year of Federal Labor and Liberal governments. The average quarter-on-quarter percentage change in Melbourne house price during the first term of Labor governments was 0.77%, slightly lower than 0.89% recorded by Liberal governments. However, at Victoria State government level, there is a notable difference, with Melbourne house prices recording a mean of 1.25% during the first year of Labor government, which is significantly higher than -0.04% recorded under the first year of Liberal rule. The major difference in performance at State government level may related to expenditure policies as Anderson *et al* (2008) argued that left-of-centre governments are more concerned with controlling unemployment than right-of-centre governments.

The Melbourne house price performance one year before an election at both Federal and Victoria State government level is shown in Table 7.

Table 7

**Federal and State Governments Last Year Election Performance  
Melbourne House Prices: Quarterly Data**

<b>Last Year</b>	Federal Labor	Federal Liberal	Federal Total	State Labor	State Liberal	State Total
Quarters	20	32	52	20	24	44
Mean	1.23%	1.19%	1.21%	3.21%	1.59%	2.33%
Std. Dev	6.23%	7.25%	6.81%	7.45%	7.46%	7.46%

Table 7 shows similarities in Melbourne house price performance at Federal and State Labor and Liberal governments one year before an election. At the Federal government level, the average quarter percentage change in Melbourne house price during the last year of a Labor government was 1.19%, slightly lower than 1.23% recorded by Liberal. At Victoria State government level, the Melbourne house price recorded a mean of 3.21% during the last year of Labor government, being close to double the 1.59%

recorded under the last year of Liberal rule. These figures are well above the long term 1.24% average for quarterly Melbourne house price performance.

For the entire data set, the quarterly performance of Melbourne house price can be compared by examining the first and last year of the elected governments. This is exhibited in Table 8.

*Table 8*

**Federal and State Governments First and Last Year Performance  
Melbourne House Prices: Quarterly Data**

<b>Mean</b>	<b>Federal Labor</b>	<b>Federal Liberal</b>	<b>State Labor</b>	<b>State Liberal</b>
First Year	0.77%	0.89%	1.25%	-0.04%
Last Year	1.23%	1.19%	3.21%	1.59%
Overall	1.08%	1.18%	1.20%	1.07%

Table 8 illustrates how Melbourne house prices perform much better in the year before an election, compared to the first year after an election. For the Federal Government, there appears to be nominal difference between the parties. Melbourne house prices overall performance was close to 50% better in the last year of government compared to the year after the election.

In analysing the results, there appears to be a strong case that political parties see house prices as a key consideration prior to an election. This is evident in both Federal and State governments. These pre-emptive policies by governments to support /stabilise house prices on the short-term could reverberate at a latter stage to inflated house prices. The long term effect on economic growth could be acutely suppressed by affordability issues across the residential property markets.

## **5. Conclusion**

This study represents a systematic empirical examination of the political cycle influence on Australian house prices. By examining the real long term performance of Melbourne established house prices to Federal and State government elections, the impact and timing of their policies can be reviewed.

Over the last four decades, quarterly Melbourne house prices increased by 1.24% (annualised return of 5.05%). There appears to be nominal variance in Melbourne house price movement between the elected Federal and State Labor and Liberal parties. The

key variation in house price movement is at election time. Melbourne house prices performance is significantly better the year before an election compared to one year post election. This is evident at both Federal and State government level, at varying degrees.

In recognising policy makers' active management of house prices for political gain, the short-term benefits of appealing to a large number of voters may conceal underlying long term flaws in the residential property market. Leaving these issues unaddressed could be more complex than often perceived.

These findings identify an array of potential areas of study. By placing political cycles as part of the residential property research agenda, those that are linked to the residential property markets should include the political framework as part of the decision making process.

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